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December 17, 2004

Mary L. Cottrell, Secretary  
Department of Telecommunications and Energy  
One South Station  
Boston, MA 02110

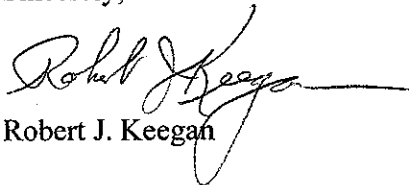
Re: D.T.E. 03-47-B (Phase II) Boston Edison Company, Cambridge Electric Light  
Company, Commonwealth Electric Company, NSTAR Gas Company,  
Pension/PBOP Adjustment Compliance Filing

Dear Ms. Cottrell:

Enclosed for filing in the above-referenced matter is the Initial Brief of Boston  
Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company  
and NSTAR Gas Company.

Thank you for your attention to this matter.

Sincerely,



Robert J. Keegan

Enclosures

cc: Caroline Bulger, Hearing Officer  
Joe Rogers, Assistant Attorney General  
Alexander Cochis, Assistant Attorney General

**COMMONWEALTH OF MASSACHUSETTS**

**DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY**

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Boston Edison Company	)
Cambridge Electric Light Company	)
Commonwealth Electric Company	)
NSTAR Gas Company	)
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D.T.E. 03-47-B (Phase II)

**INITIAL BRIEF OF BOSTON EDISON COMPANY, CAMBRIDGE ELECTRIC  
LIGHT COMPANY, COMMONWEALTH ELECTRIC COMPANY  
AND NSTAR GAS COMPANY**

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Submitted By:

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Dated: December 17, 2004

COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

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NSTAR Gas Company )  
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D.T.E. 03-47-B (Phase II)

**INITIAL BRIEF OF BOSTON EDISON COMPANY, CAMBRIDGE ELECTRIC  
LIGHT COMPANY, COMMONWEALTH ELECTRIC COMPANY  
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**I. INTRODUCTION**

On October 31, 2003, the Department of Telecommunications and Energy issued a final decision in Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company, D.T.E. 03-47-A (2003) (the "Order"), establishing an annual, reconciling adjustment factor for Boston Edison Company ("Boston Edison"), Cambridge Electric Light Company ("Cambridge"), Commonwealth Electric Company ("Commonwealth") and NSTAR Gas Company ("NSTAR Gas") (together, "NSTAR" or the "Company") to provide for the recovery of costs associated with pension and post-retirement benefits other than pensions ("PBOP"), which are not recovered through existing base rates. On December 1, 2003, the Company submitted new tariffs in accordance with the directives of the Department to: (a) establish a Pension/PBOP Adjustment Mechanism ("PAM") for each company; and (b) calculate the first annual Pension/PBOP Adjustment Factors ("PAF") to be effective as of January 1, 2004 (the "Compliance Filing"). See, D.T.E. 03-47-A, at 46-47.

On December 24, 2003, the Department issued an order determining that further investigation of the Compliance Filing would be necessary and approving the Company's compliance tariffs and pension/PBOP PAF rates for effect January 1, 2004, subject to reconciliation. Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company, D.T.E. 03-47-B (December 24, 2003). On October 4, 2004, the Department issued a Notice of Procedural Conference and Public Hearing on the Compliance Filing. The Department thereafter conducted a procedural conference on October 22, 2004 and an evidentiary hearing on December 9, 2004. The evidentiary record in D.T.E. 03-47 consists of 115 exhibits, including the testimony of witnesses on behalf of the Company and the Attorney General, and responses to information requests and record requests issued by the Company, the Department and the Attorney General in the various phases of this proceeding.<sup>1</sup>

As demonstrated by the evidence on the record, the Company's PAM tariffs and first annual PAF Filing are in full compliance with the terms of the Department's Order in D.T.E. 03-47-A and accurately account for the recovery of unamortized reconciliation deferrals existing as of December 31, 2002, allowed carrying charges, and that portion of the estimated pension and PBOP-related costs for 2003 for which recovery was allowed.

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<sup>1</sup> In total the Company has responded to three rounds of discovery in this proceeding, *i.e.*, those issued by the Department and the Attorney General in relation to the initial filing and those issued by the Department and the Attorney General in the first and second phases of the review of the Compliance Filing.

## **II. THE COMPANY'S COMPLIANCE FILING FULLY COMPORTS WITH THE TERMS OF THE DEPARTMENT'S APPROVAL IN D.T.E. 03-47-A.**

### **A. The Proposed PAM Tariffs Implement the Terms of the Department's Approval and the Company Has Accurately Calculated the PAFs To Be Effective January 1, 2004.**

In D.T.E. 03-47-A, the Department put in place a reconciling mechanism designed to recover over time the full amount of their pension and PBOP expenses (the Reconciliation Amount) and to earn a carrying charge on both the deferred Reconciliation Amount and the net prepaid pension and PBOP balances, subject to a full reconciliation of these factors yearly. To implement this decision, the Department directed the Company to file new tariffs in compliance with the directives contained in the Order. D.T.E. 03-47-A at 46-47. In the Order, the Department expressly directed that the PAM would operate as follows:

- Commencing December 1, 2003, the Company will submit a filing to reconcile (a) "SFAS-determined" pension and PBOP expenses for the prior calendar year, plus previously unamortized balances; and (b) the amount included in rates ("Reconciliation Amount") (*id.* at 45);<sup>2</sup>
- Reconciliation Amounts shall be amortized over three years (*id.*);
- Carrying costs will be allowed on the unamortized deferred pension and PBOP expenses, net of deferred income taxes, except for carrying costs associated with deferred pension and PBOP expense recorded by the Company during the first eight months of 2003 (*id.* at 46, fn.34);
- Carrying costs will be allowed on the average prepaid pension and PBOP balance net of deferred income taxes (*id.*);
- Commencing January 1, 2004, the Reconciliation Amount and carrying costs will be collected from, or refunded to, all customers on an equal cents per kilowatthour or therms basis over the following twelve months; and

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<sup>2</sup> The term "SFAS-determined" pension and PBOP expense refers to the expenses that result from the application of the Statement of Financial Accounting Standards No. 87 and 106, for pension and PBOP expenses, respectively. See D.T.E. 03-47-A, at 3.

- The Reconciliation Amount and carrying costs shall be collected through the kilowatthour delivery charge for electric distribution companies and the Local Distribution Adjustment Clause for NSTAR Gas.

As demonstrated by the extensive record in this case, the Company's Compliance Filing satisfies each of these directives. Specifically, the Compliance Filing provides a two-page exhibit that summarizes the development of the Company's PAFs for 2004 based on a preliminary estimate of PAM expenses for the period September 1, 2003 through December 31, 2003 and a forecast of kWh and MMBtus for 2004.

As shown therein, the Compliance Filing reconciles the expense amounts booked by the Company for pension and PBOP benefits in accordance with Statement of Financial Accounting Standards No. 87 ("SFAS 87") and the Statement of Financial Accounting Standards No. 106 ("SFAS 106") with the expense amount included in the Company's base rates (Compliance Filing at 1, lines 2-4) for the period September – December 2003. Further, the Compliance filing amortizes the Reconciliation Amounts over three years (Compliance Filing at 1, line 6), calculates carrying costs on the average prepaid pension balance (Compliance Filing at 1, line 19) and calculates carrying costs on Existing Reconciliation Deferrals, net of applicable deferred income taxes (Compliance Filing at 1, line 23) the unamortized deferred pension and PBOP expenses, net of applicable deferred income taxes (Compliance Filing at 1, line 27).

The PAFs calculated by the Company to implement the PAM for 2003 are designed to collect the calculated Reconciliation Amount and carrying costs from customers on an equal cents per kilowatthour or therms basis over a twelve month period commencing January 1, 2004 (Compliance Filing at 1, line 35). The Reconciliation Amount and carrying costs will be collected through the kilowatthour delivery charge for electric distribution companies and the Local Distribution Adjustment Clause for NSTAR

Gas. Thus, the Company's filing adheres strictly to the directives set forth by the Department relating to the operation of the PAM.

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In fact, the Compliance Filing is based directly on the sample calculation presented by the Company during the Department's investigation of the Company's initial filing (see, Exhibit DTE-1-4(Rev)), and incorporates the exact amounts and calculations presented in that exhibit except where necessary to institute changes expressly required by the Department's Order. As a result, the PAM ensures that customers pay no more and no less than the amounts actually needed to provide appropriate pension and PBOP benefits to the Company's employees, consistent with the Department's stated objectives in creating an annual, reconciling adjustment factor for pension and PBOP obligations.

**B. The Company's Compliance Filing is Consistent with the Department's Fitchburg Order, D.T.E. 04-48 (2004).**

The Company's Compliance Filing also addresses the Department's directives in Fitchburg Gas and Electric Light Company, D.T.E. 04-48, issued on November 1, 2004 (the "Fitchburg Order"), and therefore, no adjustments are need to implement the Department's directives in that case (Exh. AG-2-1).<sup>3</sup> In the Fitchburg Order, the Department directed FG&E to:

1. capitalize a portion of the amortization of the PBOP transition obligation in computing the 2004 reconciliation adjustment using the same capitalization ratios as for other pension and PBOP costs.
2. allocate its pension and PBOP expenses between the transmission and distribution function.

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<sup>3</sup> The Fitchburg Order generally reviewed: (1) whether Fitchburg's PAM tariffs were in compliance with Fitchburg Gas and Electric Light Company, D.T.E. 04-48 (2004); and (2) whether Fitchburg's first annual pension and PBOP adjustment was calculated accurately to become effective November 1, 2004 and January 1, 2005, for its gas and electric divisions, respectively.

3. give Fitchburg's customers credit within the carrying charge calculation for a net liability balance that existed at Unitil Services, Fitchburg's service company.
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Fitchburg Order at 22.

Consistent with the Fitchburg Order, the Company's 2003 PAF Filing already capitalizes a portion of the PBOP transition obligation by using the same capitalization ratios as for other pension and PBOP costs (Exh. AG-2-1; Tr. 1, at 8-9). As a result, the pension and PBOP capitalized amount was based on all pension and PBOP costs, including the transition obligation (Tr. 1, at 9).

In addition, the Company separately accounted for and identified the 2003 pension and PBOP costs that are related to transmission service (Exh. AG-2-1; Tr. 1, at 9-10; 85-90). Transmission-related pension and PBOP costs are collected from transmission customers in accordance with FERC-approved transmission rates through a FERC-approved labor allocator that changes the amount of pension and PBOP costs recovered in transmission rates on an annual basis (Exh. AG-2-1). The pension and PBOP costs included in base distribution rates are exclusive of the costs that are charged to transmission customers and remain fixed from year-to-year. In calculating the PAF, the Company has combined the amounts collected through transmission and distribution rates and has *deducted* both amounts as "Pension & PBOP Expense Currently in Rates" (Exh. NSTAR-1, at 1, line 3). Thus, distribution customers are receiving the full benefit of amounts charged to and collected from transmission customers. Exhibit AG-1-4



(Attachment at page 6) shows that the amounts collected through both distribution and transmission rates are incorporated in the Company's PAF calculation.<sup>4</sup>

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The Department's third directive to FG&E to include a credit to customers within the carrying charge calculation for a net liability balance at the service company level is not applicable to NSTAR because the Company has a single pension and PBOP plan as opposed to separate plans for different business entities (Tr. 1, at 10).<sup>5</sup> Accordingly, there is only one pension and PBOP prepaid balance (*id.*).

As a result, the Company's Compliance Filing fully addresses the directives of the Department as set forth in the Fitchburg Order and no further adjustments are needed or warranted to the Compliance Filing.

**C. The Compliance Filing Accurately Incorporates the Results of the Actuarial Studies Used to Calculate the SFAS-Determined Expense.**

During the discovery and evidentiary hearing process, the Attorney General sought to examine the assumptions adopted by the Company's actuaries in developing the pension and PBOP actuarial studies. Although the Company provided extensive documentation concerning its actuarial assumptions in response to the Attorney General's inquiry, this line of inquiry is misguided and irrelevant for several reasons (*see, e.g.,*

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<sup>4</sup> Mr. Farrell testified that the Company's second annual PAF Filing, dated December 7, 2004 (for effect January 1, 2005, proposed to remove transmission-related pension and PBOP costs by excluding them from 2004 Pension and PBOP distribution expense and from the amount of Pension and PBOP Expense currently in distribution rates. *See* Exhibit. NSTAR-1, 2004 Pension Adjustment Calculation at lines 3 and 4. This calculation will exclude any potential variance between transmission-related pension and PBOP expense and transmission-related pension and PBOP revenues recovered from the Company's PAF calculation (Tr. 1, at 89-90).

<sup>5</sup> In allocating the prepaid balance of the Company's pension and PBOP plan to its four distribution companies, the Company has removed from the prepaid balance amounts associated with unregulated activities as well as transmission and generation operations (Exh. AG-1-4 (Supp)).

Exh. AG 18, Exh. AG-21, Exh. AG-1-8; Exh. AG-1-9; Exh. AG-1-10, Exh. AG-1-11, Exh. AG-1-12; Exh. AG-1-20; Exh. AG-1-29).

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First, the actuarial assumptions underlying the SFAS-determined pension and PBOP expense are developed through a deliberate process in which the Company's actuaries develop the assumptions based on their expertise and industry knowledge and input from the Company (Exh. AG-23). This ensures that the assumptions are based on accurate data concerning the Company's ultimate benefit obligations to retirees and are in line with industry norms. The Company receives an actuarial statement each year related to its Pension and PBOP plans. Within this statement, the actuaries certify to the calculation of the benefit obligation and expense amount based on the Actuarial Standards of Practice of the Actuarial Standards Board. In addition, NSTAR's independent auditors examine the SFAS 87 and SFAS 106 expenses, prepaid balances and related financial statement disclosures (including all actuarial assumptions) as part of the Company's annual financial statement audit (id.). The determination of the reasonableness of the SFAS 87 and 106 expenses and prepaid balances by the Company's auditors includes an independent review of the underlying actuarial assumptions by its own actuarial experts.

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The Attorney General's inquiry also ignores the fact that: (1) under the pension/PBOP reconciliation mechanism, the Company recovers no more and no less than the amount it contributes to its SFAS 87 and SFAS 106 trust funds and any differences year to year are deferred either in the deferral or the prepaid balances and bear a carrying charge so that neither the Customers nor the Company are adversely affected by the timing differences; and (2) the year-to-year calculation of the SFAS 87

and SFAS 106 obligation inherently accounts for the differences between the actuarial assumptions and actual experience in a given year (i.e., the obligation derived under SFAS 87 and SFAS 106 in any given year is, in part, dictated by the actual experience in prior years). Each year's PAM calculation is "self-reconciling" and corrects for deviations of earlier assumptions with actual experience. This fact is clear on the record for this case:

**Q. [Brannelly] Therefore, if any projected element, i.e., assumptions of discount rates, projected medical costs, should ultimately prove different than what was actually projected, that difference, up or down, would be accounted for in a future mechanism filing; is that true?**

**A. [Farrell] That's true, because it would flow through the accounting in future periods.**

Tr. 1, at 82. Accordingly, the Attorney General's second-guessing of the actuarial assumptions underlying the SFAS-determined expense is misguided and irrelevant and should be disregarded by the Department.

### **III. CONCLUSION**

In this proceeding, the Company's proposal to establish an annual, reconciling adjustment factor to provide for the recovery of costs associated with pension and PBOP costs not recovered through existing base rates was extensively investigated and thoroughly considered by the Department, which granted approval for the mechanism on October 31, 2003. The Company's Compliance Filing provides PAM tariffs that accurately and appropriately incorporate all of the Department's directives in D.T.E. 03-47-A, and to the extent applicable, the directives set forth in the Fitchburg Order. The PAF rates that became effective January 1, 2004 are accurately calculated consistent with

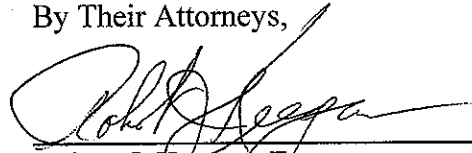
the PAM tariffs. Therefore, for all of the reasons stated above, the Company respectfully requests that the Department approve the Company's Compliance Filing.

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Respectfully submitted,

**BOSTON EDISON COMPANY  
CAMBRIDGE ELECTRIC LIGHT COMPANY  
COMMONWEALTH ELECTRIC COMPANY  
NSTAR GAS COMPANY**

By Their Attorneys,

A handwritten signature in black ink, appearing to read "Robert J. Keegan", is written over a horizontal line.

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265 Franklin Street  
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Dated: December 17, 2004

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